

**Tax Supported
New Issue**

State of Idaho

Ratings

New Issue Tax Anticipation Notes, Series 2008	F1+
Outstanding Debt Tax Anticipation Notes, Series 2007	F1+

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New Issue Details

Sale Information: \$600,000,000 Tax Anticipation Notes, Series 2008, the week of June 16 via negotiation.
Security: An irrevocable pledge of taxes and other revenues received by Idaho in the fourth quarter of fiscal 2009, borrowable resources to the extent necessary, and the state's faith and credit pledge.
Purpose: Finance operating purposes during the fiscal year ending June 30, 2009.
Final Maturity: June 30, 2009.

Related Research

- [State of Idaho, June 13, 2007](#)

Rating Rationale

- The series 2008 tax anticipation notes bear faith and credit of Idaho with holdbacks employed, if necessary, to ensure payment.
- Good coverage exists from a first claim on fourth-quarter general fund revenues equal to 1.67x note principal.
- Coverage is broadened by available borrowable reserves to 4.2x note principal.
- Surplus balances are fully funded and are now close to 14% of revenues.
- The pace of economic growth has slowed, with projected revenues and ending cash balances reduced.
- Tax relief led to a permanent 1% increase in sales tax, as the state assumed a larger share of education funding and accelerated the distribution of education aid requiring enlarged cash deficits offset by rising external and internal borrowing.

Key Rating Drivers

- Further payment shifts that would enlarge cash deficits in the beginning of the fiscal year, potentially reducing coverage from pledged revenues.

Credit Summary

The 'F1+' rating reflects the security provided for the notes by an irrevocable pledge of taxes and other revenues received by the state in fourth-quarter fiscal 2009, borrowable resources to the extent necessary, and the state's faith and credit pledge. Fourth-quarter projected fiscal 2009 revenues are \$999.8 million. Pledged revenues provide 1.7x coverage of note principal, the cash flow safety margin is 1.8%, and borrowable resources provide 4.0x coverage of note principal. Additionally, the state has a practice of reducing spending as necessary through holdbacks to ensure sufficient funds for note repayment.

Legislation enacted in the middle of fiscal 2007 accelerated the payment of school aid to provide property tax relief, as the state now provides 79% of education funding. The sales tax was raised 1% (fiscal 2008 was the first full year at the 6% rate). As a result of the change in education aid, more than 81% of it is disbursed in the first five months of fiscal 2009. The effect of this legislative change enlarged cash flow imbalances and the need to borrow more internally and externally. Timing differences between revenue collections and disbursements result in projected negative general fund cash balances in almost every month throughout fiscal 2009. The operating borrowing is necessary, as 35% of fiscal year revenue is collected in the fourth quarter.

Pledged revenues are deposited into the note repayment account. Once made into the account, deposits cannot be withdrawn or loaned back to the general fund. Deposits for fiscal 2008 notes due June 30, 2008 were made earlier, between March 2008 and May 2008, to provide for the repayment of \$400 million of external notes and \$49.3 million of internal notes. Fiscal 2009 revenues have been revised to reflect the current sluggish economic conditions and legislative changes for tax relief. Total general fund revenues are now projected to rise 2.8% from fiscal 2008 levels, with a base sales tax growth of 4.9%. Following the projected 1.5% decline in fiscal 2008,

Rating History

Rating	Action	Outlook/ Watch	Date
F1+	Assigned	—	6/13/08

personal income tax receipts are projected to rise 0.4% in fiscal 2009. After note repayment, the projected general fund cash balance on June 30, 2009 is \$54.5 million, down from the \$191.8 million projected at June 30, 2008. The lowered ending balance reflects spending for statutory transfers and increased education aid to provide property tax relief. The state has built up its reserves, which, on a combined basis, equal almost 14% of spending. The budget stabilization fund is projected to hold \$140.6 million on June 30, 2009, with another \$68.9 million held in the economic recovery reserve fund. The property tax relief act of 2006 funded a \$100 million public education stabilization reserve, which is expected to close fiscal 2009 with \$116.5 million. Borrowable resources are substantial at \$2.4 billion, equal to 4.0x coverage of fiscal 2009 note principal and 2.4x coverage of fiscal 2009 fourth-quarter revenues.

Notes

The notes are issued pursuant to the state constitution and chapter 32, title 63 of the Idaho Code (the act). The act limits borrowing to 75% of taxes reasonably anticipated to be collected for the fiscal year. In fiscal 2009, tax receipts are estimated for at least \$2.85 billion, resulting in a limit of \$2.14 billion. The state does not anticipate another external borrowing for fiscal 2009 but expects internal borrowing of about \$270.3 million to meet the midyear operating low point of negative \$870.3 million. To support fiscal 2008 cash flow, the state issued \$400 million of external notes and \$49.3 million of internal notes (periodically the state has issued internal notes). Following legislative changes in fiscal 2007 to accelerate school funding, the state borrowed \$100 million externally and internally borrowed \$170 million. Prior to fiscal years' 2008 and 2007 internal borrowing, the state had issued internal notes in fiscal 2003, when \$130 million was required. Outstanding series 2007 external notes to support fiscal 2008 cash flow are due June 30, 2008, and funds were impounded between March 2008 and April 2008 in amounts sufficient to repay both internal and external notes.

Idaho will borrow \$600 million, or 19.6% of cash flow, for operating purposes during fiscal 2009. The state issues operating notes annually in varying amounts. This issuance is the largest the state has had and reflects enlarged borrowing due to the change in the distribution of education aid. In fiscal 2004, the state issued \$375 million in notes to support cash flow during the economic downturn occurring at that time. With the accelerated disbursement of state school aid, 81% of state education aid is paid during the first five months of the fiscal year. In contrast, about 34% of state tax revenues are received in the fourth quarter of the fiscal year.

The series 2008 notes are secured by an irrevocable pledge of taxes and other revenues received by the state in fourth-quarter fiscal 2009 from borrowable resources and the state's faith and credit pledge. The notes are not general obligations. Fourth-quarter revenues, as they are received by the state, are deposited into a note payment account until the balance is sufficient to pay the principal and interest on the notes and are irrevocably appropriated and set aside solely for note payment. Funds in the note account may only be invested in direct obligations of the federal government and certain fully collateralized time certificates of deposit and repurchase agreements permitted under the state code.

Finances

The state's general fund budgeting and accounting are on a cash basis, although comprehensive annual financial reports in conformance with generally accepted accounting principles (GAAP) have been issued since fiscal 1996. Individual and corporate income and sales tax collections now account for about 89% of revenues.

The state's revenue forecasting, monitoring, and budget control mechanisms are excellent. The executive revenue forecast is made in January, six months prior to the start of the fiscal year, and forms the basis of the budget. A second forecast occurs after the commencement of the fiscal year, and a third midyear reforecast occurs in January. A joint legislative committee reviews the executive revenue forecast. A broad-based revenue monitoring group consisting of the executive and legislative branches reviews actual receipts and projections monthly. The state Legislature and governor are constitutionally responsible for achieving a balanced budget, and the governor uses across-the-board holdbacks of appropriations, when necessary, to achieve balance.

Reflecting strong revenue growth and conservative financial management practices, unobligated general fund balances grew between fiscal years 1999 and 2001, to \$182.7 million from \$46.6 million. At the same time, the state added to the budget stabilization fund, resulting in a balance of \$73 million at the start of fiscal 2002. The buildup of this financial cushion allowed the state to weather the economic and financial downturn that took hold during fiscal 2002. Revenues in fiscal 2002 declined 14.3% and were revised downward several times. About one-half the reduction can be attributed to changes in the law, particularly adjustments to the individual income tax, with the remainder reflecting lowered collections due to the weakening economic environment. However, the extent of the recession required the state in fiscal 2003 to exhaust its fund balances, reduce appropriations, and institute one-time transfers of \$193 million into the general fund. The general fund closed with a \$15.7 million unobligated balance on June 30, 2003.

In the past four fiscal years, the state has effectively replaced the one-time measures with a similar amount of tax increases, including the now permanent 1% sales tax hike and a permanent increase in the cigarette tax. These measures helped fund increased education aid to provide \$250 million property tax relief per enacted legislation for school building repairs, to resolve school finance litigation. This change does not increase education funding. However, the state's share of education funding has risen to 79.5% from 65.0% by replacing the local maintenance and operating property tax levy with the state's 1% sales tax increase and \$50 million of surplus balances. The fiscal 2008 budget included an additional \$5 million in funds for school maintenance to meet capital requirements for school funding under the state Supreme Court ruling. Another \$25 million was available under a school district loan program.

Revenue projections for fiscal years 2008 and 2009 have been revised to reflect slower economic growth in the real estate sector, leading to reductions in projected revenue growth. For the first 10 months of fiscal 2008 (through April 30, 2008), total general fund revenues rose 2%, with a 3.3% rise in personal income tax receipts and a 1.3% decline in sales tax collections from projected levels. The ending general fund balance as of June 30, 2008 is projected to reach \$191.8 million. April 2008 nonfarm employment rose only 0.2%, below the 0.3% rise for the U.S. and well below the state's employment gains of 2.7% and 4.4% in 2007 and 2006, respectively. Personal income rose 6.8% in 2007, equal to 110% of the national level. By measure of personal income per capita, the pace of state growth was slower, rising 4.3%, to 83% of the national level. Personal income per capita ranks the state 44th in the nation.

The budget for fiscal 2009 anticipates general fund revenue growth of 2.8%, including a 0.4% rise in personal income tax collections, up from fiscal 2008's projected 1.8% decline from the prior year. Sales tax collections are slated to only increase 4.9% following an 8.2% surge in fiscal 2008. Revenue measures include tax relief of \$66.4 million and reflect an increase in the grocery tax credit of \$22.3 million and \$38 million to conform federal tax treatment of the economic stimulus package. Outflows include \$38.4 million in fund transfers including water board, scholarship, and permanent building funds. The fiscal 2009

estimated beginning balance of \$176.9 million is projected to be drawn to \$54.5 million and include \$39.1 million of appropriation spending reductions. The budget stabilization fund has steadily been replenished and is expected to hold \$140.6 million as of June 30, 2009. Under GAAP, the fiscal 2007 unreserved fund balance of \$996 million was equal to 31.8% of revenues, up from \$324 million, or 17.9% of revenues, in fiscal 2002.

Cash Flow

As of June 30, 2009, total revenues amount to \$2.9 billion, with \$3 billion in expenses, for an ending balance of \$54.6 million that covers note repayment 1.1x. Timing differences between revenue collections and disbursements result in negative balances in 10 months of the fiscal year. Due to legislation accelerating disbursement of educational aid, negative balances before borrowing are forecast to occur in almost every month of the year. The maximum deficit in fiscal 2009 occurs in November 2008, when the negative balance is estimated at \$870.3 million. In addition to the series 2008 notes, the state has the ability to issue internal notes, whereby the general fund borrows moneys from other state funds and accounts. These notes, which typically are outstanding for periods of 12–66 days and repaid before the close of the fiscal year, were issued in fiscal years 2007 and 2008 following the disbursement changes.

Approximately 33% of the year's revenues are received in the first five months of the fiscal year, with disbursements equal to 63% occurring during this period. The state supports 79% of school spending, equal to \$1.41 billion in fiscal 2009, or 47% of general fund spending. With legislative changes, 81% of such payments are disbursed over the first five months of fiscal 2008. In fiscal 2007, such amounts represented about 61%. The new disbursement schedule provides for 30% of aid to be disbursed in August and October, 20% in November, and 10% each in February and May.

The three major taxes are individual income, corporate income, and sales taxes, which together make up 95% of general fund revenues. The individual income tax makes up about 47% of general fund revenues, fairly consistent with prior years, with 37% estimated to be collected in the first one-half of fiscal 2009. Sales tax collections received in the first one-half of the fiscal year are projected to be 48%. At 35%, the bulk of the fiscal year's collections are accounted for in the fourth quarter, allowing for a \$54.6 million positive ending cash balance for the fiscal year ending June 30, 2009, when the notes are paid. In past years, to accommodate smaller balances the state identified unbudgeted resources that were available to support financial operations. Furthermore, across-the-board appropriation holdbacks are used as necessary, including in fiscal years 2002 and 2003, to achieve balance. However, the requirement of first moneys applied to note repayment is an important offsetting risk factor, as are the ample borrowable funds.

Coverage by fourth-quarter fiscal 2009 pledged revenues of \$999.8 million provides 1.7x coverage of the \$600 million external notes. While note payment fund deposits are not required until the beginning of the fourth quarter (April 1), deposits have been made earlier in prior years. For the outstanding \$400 million notes due June 30, 2008, deposits to the note account were made between April 2008 and May 2008. In March 2008, some \$49.3 million of internal borrowing was repaid. While early deposits are discretionary, once made they cannot be withdrawn or loaned back to the general fund. Given enlarged borrowing due to the acceleration of education aid, coupled with slower growth in revenues, payments prior to April are not as likely to be made in future years.

A month-end general fund cash balance of negative \$166.2 million for May 2009 is forecast. However, substantial borrowable funds are available until the balance of projected revenues is collected by fiscal year end to generate the June 30 balance. Borrowable

resources were projected to be \$2.65 billion on May 30, 2008, or 16.0x the May 30 cash balances and 2.7x the fourth-quarter cash flow. Relative to the \$600 million of external notes, borrowable resources provide an additional 4.02x principal coverage of the notes at fiscal year end. The \$600 million of notes represents 20.9% of revenues or 19.6% of cash flow, with the cash flow safety margin a satisfactory 1.8%.

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